KPMG

FOOTHILL/EASTERN TRANSPORTATION
CORRIDOR AGENCY

Financial Statements

June 30, 2015

(With Independent Auditors' Report Thereon)

FOOTHILL/EASTERN TRANSPORTATION
CORRIDOR AGENCY

Table of Contents

KPMG LLP
Suite 700
20 Pacifica
Irvine, CA 92618-3391

Independent Auditors' Report

The Honorable Board of Directors
Foothill/Eastern Transportation Corridor Agency:

We have audited the accompanying financial statements of the Foothill/Eastern Transportation Corridor Agency (the agency), which comprise the statement of net position as of June 30, 2015, and the related statements of revenue, expenses, and changes in net position and cash flows for the year then ended, and the related notes to the financial statements.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Foothill/Eastern Transportation Corridor Agency as of June 30, 2015, and the results of its operations and its cash flows for the year then ended in accordance with U.S. generally accepted accounting principles.

Emphasis of Matters

Adoption of New Accounting Pronouncements

As discussed in the *Significant Accounting Policies* note to the financial statements, in 2015 the agency adopted Governmental Accounting Standards Board (GASB) Statement No. 68, *Accounting and Financial Reporting for Pensions* and GASB Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date*. Our opinion is not modified with respect to this matter.

Other Matter

Required Supplementary Information

U.S. generally accepted accounting principles require that management's discussion and analysis on pages 3–8 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

KPMG LLP

October 2, 2015

This discussion and analysis of the financial performance of the Foothill/Eastern Transportation Corridor Agency (the agency) provides an overview of the agency's financial activities for the fiscal years ended June 30, 2015 and 2014. Please read it in conjunction with the agency's financial statements and accompanying notes.

Background

The agency was formed in 1986 as a joint powers authority by the County of Orange and cities in Orange County, California to provide traffic relief to Orange County through the construction and operation of toll roads. The agency was created to plan, design, finance, construct, and operate the Foothill (State Route 241) and Eastern (State Route 241, State Route 261, and State Route 133) Toll Roads. The agency's primary focus is the operation of the facilities and collection of tolls to repay the tax-exempt revenue bonds that were issued to construct the toll roads.

Planning began in the 1970s when local transportation studies identified the need for new highways, including the Foothill and Eastern Transportation Corridors (State Route 241, State Route 261, and State Route 133), to serve Orange County's growing population. In the early 1980s, the corridor was envisioned as a free highway funded through state or federal gas-tax revenue, but with a shortage of gas-tax revenue to fund transportation improvements and increasing costs of building new roads, local officials began to study alternative ways to fund road projects.

In the mid-1980s, two state laws were passed authorizing the agency to collect tolls and development impact fees to fund road construction. With a pledged revenue stream from future tolls and development impact fees, the agency issued nonrecourse, toll-revenue bonds to fund road construction, rather than relying on the uncertainty of state gas-tax revenue. The agency also reached an agreement with the California Department of Transportation (Caltrans) to assume ownership, liability, and maintenance of the State Route 241, State Route 261, and State Route 133 Toll Roads as part of the state highway system. This agreement eliminated the need for the agency to seek additional funding sources for road maintenance.

In 1993, the first 3.2-mile segment of the Foothill (State Route 241) Toll Road opened to traffic, the first toll road in Southern California to use FasTrak®, an electronic toll collection system that allowed drivers to pay tolls without stopping at a toll booth. At June 30, 2015 and 2014, averages of approximately 193,000 and 177,000 transactions were recorded on the State Route 241, State Route 261, and State Route 133 Toll Roads every weekday, serving as an important, time-saving alternative route to local freeways and arterial roads.

Financial Highlights

Tolls, fees, and fines collected in fiscal year 2015 (FY15) totaled $149,902 compared to $138,923 in fiscal year 2014 (FY14), an increase of 7.9%.

As of June 30, 2015 and 2014, the agency had $403,780 and $517,347, respectively, in restricted cash and investments that were subject to master indentures of trust for the bonds outstanding at each date. In February 2015, the agency issued $87,008 of Senior Lien Toll Road Refunding Revenue Bonds; together with a portion of restricted cash and investments, the proceeds of the issuance were used to refund the previously unrefunded portion of its Series 1995A Senior Lien Toll Road Revenue Bonds. The agency also had $151,348 and $129,990 of unrestricted cash as of June 30, 2015 and 2014, respectively.

(Continued)

(In thousands)

The agency's net position at June 30, 2015 and 2014 was $ (1,456,090) and $ (1,453,701), respectively. The negative net position results primarily from the inclusion in the agency's financial statements of its long-term debt obligations, which were used to fund construction of the corridors, but not the related capital assets, since ownership of the corridors was transferred to Caltrans upon completion.

Overview of the Financial Statements

The agency's financial statements include the statement of net position, statement of revenue, expenses, and changes in net position, statement of cash flows, and notes to the financial statements. The financial statements present the financial picture of the agency from the economic resources measurement focus using the accrual basis of accounting. These statements include the assets and liabilities of the agency as well as certain items labeled as deferred outflows and inflows of resources. The current year's revenue and expenses are taken into account regardless of when cash is received or paid. The statement of cash flows provides information about the agency's cash receipts, cash payments, and net changes in cash resulting from operating, capital and related financing, and investing activities during the reporting period.

The statement of net position and the statement of revenue, expenses, and changes in net position report the agency's net position and related changes. Net position is the difference between the total of recorded assets and deferred outflows and the total of liabilities and deferred inflows. The recorded activities include all toll revenue and operating expenses related to the operation of the Foothill/Eastern Transportation Corridors, as well as the agency's construction-related activities and related financing costs. Activities are financed by toll revenue, development impact fees, fees and fines, and investment income.

Financial Analysis

The following table summarizes the net position of the agency as of June 30, 2015 and 2014:

	2015	2014	Percentage increase (decrease)
Assets and deferred outflows:			
Current assets	$ 227,001	269,020	(15.6)%
Capital assets, net	285,666	384,343	(25.7)
Other noncurrent assets	467,303	394,047	18.6
Deferred outflows	13,284	13,822	(3.9)
Total assets and deferred outflows	993,254	1,061,232	(6.4)
Liabilities and deferred inflows:			
Bonds payable	2,353,039	2,423,519	(2.9)%
Net pension liability	7,556	—	—
Other liabilities	87,738	91,414	(4.0)
Deferred inflows	1,011	—	—
Total liabilities and deferred inflows	2,449,344	2,514,933	(2.6)
Net position	$ (1,456,090)	(1,453,701)	0.2

As more fully described in notes 5 and 7(e) to the accompanying financial statements, the decrease in capital assets from FY14 to FY15 reflects the reclassification of $120,000 of payments made to the San Joaquin Hills Transportation Corridor Agency (SJHTCA) through 2009 that were originally recorded as construction in progress related to the 241 completion project. In connection with SJHTCA's November 2014 bond refinance transaction, the agency's Board of Directors and SJHTCA's Board of Directors approved an agreement that provided for termination of the Mitigation Payment and Loan Agreement between the agencies, concurrently with the closing of the transaction. The termination agreement also provided for SJHTCA to pay $120,000 to the agency, in annual installments beginning January 15, 2025 equal to 50% of SJHTCA's surplus funds, plus accrued interest. Accordingly, this amount has been recorded during FY15 as a note receivable from SJHTCA and a reduction of construction in progress.

The decrease described above was partially offset by the costs of continuing work in connection with the 241 Tesoro Extension that will lengthen the 241 by 5.5 miles, including the development of engineering plans, completion of environmental assessments, ongoing outreach and community input, and development of a financial strategy for the extension. When completed, the 241 Tesoro Extension will provide a valuable alternative route for commuters and residents in the surrounding area. Long-range planning efforts also continued related to the 241 completion project.

The category above labeled deferred outflows includes two components: the first is the amount by which the reacquisition price of the bonds refunded in FY14 exceeded their net carrying value. This amount has been deferred and is being amortized over the remaining period during which the refunded bonds were scheduled to be paid. In addition, as more fully described in notes 2 and 8 to the accompanying financial statements, the agency adopted Governmental Accounting Standards Board (GASB) Statement No. 68 in FY15 and recorded its proportionate share of the collective net pension liability applicable to the defined benefit pension plan in which its employees participate, as well as related deferred outflows and inflows of resources related to pensions. This resulted in an adjustment to the agency's previously reported net position as of June 30, 2014 in order to record its net pension liability as of that date, as reflected in the statement of revenue, expenses, and changes in net position.

(Continued)

(In thousands)

Following is a summary of the agency's revenue, expenses, and changes in net position for the years ended June 30, 2015 and 2014:

		2015	2014	Percentage increase (decrease)
Operating revenue:				
Tolls, fees, and fines	$	149,902	138,923	7.9%
Development impact fees		24,901	19,813	25.7
Other revenue		386	396	(2.5)
Grant revenue		—	14	(100.0)
Total operating revenue		175,189	159,146	10.1
Operating expenses		24,979	24,066	3.8
Operating income		150,210	135,080	11.2
Nonoperating expenses, net		(144,560)	(155,693)	(7.2)
Change in net position		5,650	(20,613)	
Net position at beginning of year		(1,453,701)	(1,433,088)	1.4
Adjustment for the cumulative effect on prior years of applying retroactively the new method for accounting for pensions		(8,039)	—	—
Net position at end of year	$	(1,456,090)	(1,453,701)	0.2

Revenue for the agency consists primarily of tolls, fees, and fines, which comprised 85.6% of total revenue in FY15 compared to 87.3% of total revenue in FY14. Tolls, fees, and fines increased by 7.9% over each of the two preceding years, primarily due to toll rate increases and increases in toll transactions. Development impact fees were $24,901 in FY15 and $19,813 in FY14, an increase of 25.7%, compared to an increase of 68.0% in FY14. The amounts of development impact fees collected fluctuate from year to year depending on residential and nonresidential development in Orange County within the area of benefit.

Operating expenses were $24,979 in FY15 compared to $24,066 in FY14, an increase of 3.8%. Included in operating expenses in FY15 is noncash depreciation expense on fixed assets of $4,902, compared to $2,277 in FY14. The increase in depreciation expense is attributable to the completion of the agency's All Electronic Tolling (AET) project in FY15. Excluding depreciation, operating expenses were $20,077 in FY15 and $21,789 in FY14, a decrease of $1,713.

Net nonoperating expenses for FY15 include investment income of $11,692; interest expense of $142,388; $11,684 related to the cost of capital improvements contributed to Caltrans; and two items related to its FY15 long-term debt refinancing transaction: costs of $2,061 that were paid and recorded as expense, and amortization of $119 related to additional costs that were deferred on the agency's balance sheet. For FY14, the agency had a loss of

(Continued)

(In thousands)

$434 on the disposition of capital assets; investment income of $8,019; interest expense of $140,623; $1,729 related to the cost of capital improvements contributed to Caltrans; expenses of $20,890 related to its FY14 long-term debt refinancing transaction; and amortization of $36 related to additional transaction costs that were deferred. Accrual basis interest expense included accretion on the agency's capital appreciation bonds and convertible capital appreciation bonds of $22,086 and $35,142 in FY15 and in FY14, respectively. Interest expense in FY15 and FY14 also included noncash amortization of $416 and $194, respectively, related to a discount on the issuance of bonds and of $1,414 and $712, respectively, related to the deferred bond refunding costs.

Capital Assets, Net

The following table summarizes the agency's capital assets, net of accumulated depreciation, at June 30:

		2015	2014
Construction in progress	$	247,802	346,643
Right-of-way acquisitions, grading, or improvements		15,014	15,014
Furniture and equipment		22,850	22,686
Total capital assets	$	285,666	384,343

Construction in progress includes expenditures related to the All Electronic Tolling (AET) project prior to its completion in FY15 and improvements in progress related to the 241 completion project. Right-of-way acquisitions, grading, or improvements include easements and environmental mitigation parcels. Furniture and equipment includes facility and toll revenue equipment related to the corridor operations facility, transponders, toll and violations collection equipment, buildings, and changeable message signs.

More detailed information about the agency's capital assets is presented in note 5 to the financial statements.

Debt Administration

The agency had outstanding bonds payable of $2,353,039 and $2,423,519 at June 30, 2015 and 2014, respectively. The changes in FY15 and FY14 are attributable to the accretion of principal on capital appreciation bonds of $22,086 and $35,142, respectively, and to the bond refunding transactions completed in each year.

(Continued)

All of the agency's toll, fees, fines and development impact fee revenue, less certain expenses, as defined in the indentures of trust, is pledged to repay these bonds. The agency has several debt covenants contained in the master indentures of trust. Management of the agency represents that the agency was in compliance with all of its covenants as of and for the years ended June 30, 2015 and 2014.

Economic Factors

After consideration of toll rate recommendations from the agency's traffic consultant and the potential effects of traffic diversion, toll rates were approved by the agency's Board of Directors for implementation effective July 1, 2015. The new toll rates are projected to result in a 3.4% increase in transactional toll revenue and reflect increases of 2% for FasTrak® toll rates and maintenance of the $1.00 increment above the FasTrak® rates for non-FasTrak transactions.

The agency continues to focus on customer incentives and promotions to attract new drivers, reward current customers, and increase total transactions and revenue.

Contacting the Agency's Financial Management

This financial report is designed to provide a general overview of the agency's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to the Controller, Foothill/Eastern Transportation Corridor Agency, 125 Pacifica, Suite 100, Irvine, CA 92618 or to info@thetollroads.com.

FOOTHILL/EASTERN TRANSPORTATION CORRIDOR AGENCY

Statement of Net Position

June 30, 2015

(In thousands)

Assets:		
Current assets:		
Cash and investments	$	76,833
Restricted cash and investments		141,926
Receivables:		
Accounts, net of allowance of $2,639		4,395
Fees		936
Interest		1,436
Other assets		1,475
Total current assets		227,001
Noncurrent assets:		
Cash and investments		74,515
Restricted cash and investments		261,854
Capital assets, net		285,666
Unamortized prepaid bond insurance		10,739
Note receivable – San Joaquin Hills Transportation Corridor Agency		120,195
Total noncurrent assets		752,969
Deferred outflows of resources:		
Unamortized deferral of bond refunding costs		12,407
Pension costs		877
Total assets and deferred outflows		993,254
Liabilities:		
Current liabilities:		
Accounts payable		10,975
Unearned revenue		18,196
Due to San Joaquin Transportation Corridor Agency		6,444
Employee compensated absences payable		411
Interest payable		51,712
Total current liabilities		87,738
Net pension liability		7,556
Long-term bonds payable		2,353,039
Total liabilities		2,448,333
Deferred inflows of resources:		
Pension costs		1,011
Total liabilities and deferred inflows		2,449,344
Net position:		
Net investment in capital assets		(1,924,032)
Restricted		325,273
Unrestricted		142,669
Total net position	$	(1,456,090)

See accompanying notes to financial statements.

FOOTHILL/EASTERN TRANSPORTATION CORRIDOR AGENCY

Statement of Revenue, Expenses, and Changes in Net Position

Year ended June 30, 2015

(In thousands)

Operating revenue:		
Tolls, fees, and fines		$ 149,902
Development impact fees		24,901
Other revenue		386
Total operating revenue		175,189
Operating expenses:		
Toll compliance and customer service		11,673
Depreciation		4,902
Salaries and wages		2,907
Toll systems		1,566
Marketing		1,410
Insurance		773
Toll facilities		739
Professional services		612
Facilities operations, maintenance and repairs		174
Other operating expenses		223
Total operating expenses		24,979
Operating income		150,210
Nonoperating revenue (expenses):		
Investment income		11,692
Contribution of capital improvements to Caltrans		(11,684)
Costs of bond refunding		(2,061)
Amortization of prepaid bond insurance		(119)
Interest expense		(142,388)
Nonoperating expenses, net		(144,560)
Change in net position		5,650
Net position at beginning of year, as previously reported	(1,453,701)	
Adjustment for the cumulative effect on prior years of change in accounting principles for pensions (note 2(b))	(8,039)	
Net position at beginning of year, as adjusted		(1,461,740)
Net position at end of year		$ (1,456,090)

See accompanying notes to financial statements.

FOOTHILL/EASTERN TRANSPORTATION CORRIDOR AGENCY

Statement of Cash Flows

Year ended June 30, 2015

(In thousands)

Cash flows from operating activities:		
Cash received from toll road patrons	$	152,022
Cash received from development impact fees		23,985
Cash received from other revenue		386
Cash payments to suppliers		(15,796)
Cash payments to employees		(2,706)
Net cash provided by operating activities		157,891
Cash flows from capital and related financing activities:		
Cash payments for acquisition of capital assets		(38,095)
Cash paid in connection with bond refunding transaction		(96,403)
Cash payments for interest and principal		(127,043)
Net cash used for capital and related financing activities		(261,541)
Cash flows from investing activities:		
Cash receipts for interest and dividends		8,578
Cash receipts from the maturity and sale of investments		441,441
Cash payments for purchase of investments		(310,108)
Net cash provided by investing activities		139,911
Net increase in cash and cash equivalents		36,261
Cash and cash equivalents at beginning of year		93,346
Cash and cash equivalents at end of year (note 4)	$	129,607
Reconciliation of operating income to net cash provided by operating activities:		
Operating income	$	150,210
Adjustments to reconcile operating income to net cash provided by operating activities:		
Depreciation		4,902
Changes in operating assets and liabilities:		
Accounts receivable		(1,003)
Fees receivable		(916)
Due to San Joaquin Hills Transportation Corridor Agency		1,342
Other assets		(34)
Accounts payable		1,408
Unearned revenue		1,781
Net pension liability and related accounts		(349)
Employee compensated absences payable		550
Total adjustments		7,681
Net cash provided by operating activities	$	157,891

(Continued)

FOOTHILL/EASTERN TRANSPORTATION CORRIDOR AGENCY

Statement of Cash Flows

Year ended June 30, 2015

(In thousands)

Noncash capital and related financing and investing activities:		
Bond refunding, including the following elements:		
Proceeds of new bonds issued	$	87,008
Escrow deposit to repay principal on refunded bonds		(179,990)
Transaction costs charged to expense		(2,061)
Prepaid bond insurance		(1,360)
Interest expense recorded for accretion of bonds outstanding		(22,086)
Amortization of bond discount recorded as interest expense		(416)
Amortization of deferred bond refunding cost recorded as interest expense		(1,414)
Amortization of prepaid bond insurance		(119)
Contribution of capital improvements to Caltrans		(11,684)
Interest accrued on note receivable from San Joaquin Hills Transportation Corridor Agency		195
Change in unrealized gain/loss on investments		5,490
Amortization of discount/premium on investments		(2,629)

See accompanying notes to financial statements.

(1) Reporting Entity

In recognition of the regional transportation needs in the County of Orange (County), the California State Legislature enacted various amendments to the California Government Code to authorize the financing of bridges and major thoroughfares by joint powers agencies. Pursuant to such authorization, the Foothill/Eastern Transportation Corridor Agency (the agency) was created in January 1986 by a joint exercise of powers agreement. Current members are the County and the cities of Anaheim, Dana Point, Irvine, Lake Forest, Mission Viejo, Orange, Rancho Santa Margarita, San Clemente, San Juan Capistrano, Santa Ana, Tustin, and Yorba Linda (collectively, the member agencies). The purpose of the agency is to plan, design, construct, finance, administer funds for, and operate the Foothill and Eastern Transportation Corridors. The agency is governed by a Board of Directors comprising representatives from the member agencies. The agency has the power to, among other things, incur debt and establish and collect tolls.

The financial statements comprise the activities of the agency. There are no other organizations for which the agency is financially accountable or for which it is fiscally responsible. The agency and the San Joaquin Hills Transportation Corridor Agency (SJHTCA) are under common management and together are called the Transportation Corridor Agencies. However, each agency has an independent governing board.

(2) Summary of Significant Accounting Policies

The accounting policies of the agency are in conformity with U.S. generally accepted accounting principles (U.S. GAAP) applicable to governmental units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing accounting and financial reporting principles.

(a) Basis of Presentation

The agency records revenue in part from fees and other charges for services to external users and, accordingly, has chosen to present its financial statements using the reporting model for special-purpose governments engaged in business-type activities. This model allows all financial information for the agency to be reported in a single column in each of the accompanying financial statements.

The agency distinguishes operating revenue and expenses from nonoperating items in the preparation of its financial statements. Operating revenue and expenses generally result from the collection of tolls, fees, and fines on the corridors. The agency's operating expenses include depreciation, materials, services, and other expenses related to the operation of the corridors. All revenue and expenses not meeting this definition are reported as nonoperating revenue and expenses.

(b) Basis of Accounting

The financial statements are prepared using the accrual basis of accounting. Revenue is recognized when earned, and expenses are recognized when incurred. During the year ended June 30, 2015, the Agency implemented GASB Statements No. 68, *Accounting and Financial Reporting for Pensions – An Amendment of GASB Statement No. 27* and No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date – An Amendment of GASB Statement No. 68.*

Restricted resources are used in accordance with the agency's master indentures of trust. Unrestricted resources are used at the agency's discretion. When both restricted and unrestricted resources are available for use, it is the agency's policy to determine on a case-by-case basis when to use restricted or unrestricted resources.

(c) Budget

Fiscal year budgets are prepared by the agency's staff for estimated revenue and expenses. The Board of Directors adopts the annual budget at the June board meeting for the fiscal year commencing the following July. The approval of the budget requires the consent of at least two-thirds of the board members. No expenditures in excess of the total budget for each board-designated category are made without the approval of at least two-thirds of the board members, at which time a revised and amended budget is required to be submitted to the Board of Directors. All budgets are adopted on a basis consistent with U.S. GAAP. All budget appropriations lapse at year-end. Any budgeted expenses not incurred by each year-end must be reappropriated in the next fiscal year.

(d) Cash and Cash Equivalents

Cash and cash equivalents generally consist of cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition.

(e) Investments

Investments are stated at fair value, generally based on quoted market prices.

The agency classifies investments as current or noncurrent based on how readily the investment is expected to be converted to cash and whether any restrictions limit the agency's ability to use the resources.

(f) Receivables

Receivables include amounts due from member agencies for development impact fees collected on behalf of the agency, credit card receivables, interoperable receivables due from other California toll agencies, receivables from patrons for violations and tolls, and interest.

(g) Capital Assets

Capital assets include construction in progress, environmental mitigation sites, easements, the corridor operations facility, transponders, toll and violations collection equipment, buildings, changeable message signs, vehicles, and furniture. Capital assets are defined by the agency as assets with an initial individual cost of more than five thousand dollars, with the exception of transponders that are valued in total, and an estimated useful life in excess of one year.

As described further in note 5, the Foothill/Eastern Transportation Corridors and the related purchases of rights of way, for which title vests with the California Department of Transportation (Caltrans), are not included as capital assets because the agency does not have title to these assets. The costs of normal maintenance and repairs and mitigation that do not add value to the assets or materially extend asset lives are not capitalized.

Capital assets are recorded at cost and are depreciated using the straight-line method over the following estimated useful lives:

Asset type	Useful life
Buildings	20–30 years
Changeable message signs	15 years
Toll revenue equipment	5 years
Vehicles	5 years
Leasehold improvements, other equipment, and furniture	5–10 years

Assets determined to be impaired are recorded at the lower of cost or estimated net realizable value.

(h) Unearned Revenue

Unearned revenue represents prepaid tolls collected from patrons, including those using FasTrak®, an electronic toll collection system.

(i) Unamortized Deferral of Bond Refunding Costs

Deferred bond refunding costs represent certain costs related to the issuance of bonds. These costs have been recorded as deferred outflows of resources, and are being amortized over the remaining period during which the refunded bonds were scheduled to be repaid, as more fully detailed in note 6.

(j) Pension Plan

Qualified permanent employees of the agency participate in a cost-sharing multiple-employer defined benefit pension plan administered by the Orange County Employees Retirement System (OCERS). For purposes of measuring the agency's net pension liability, deferred outflows/inflows of resources related to pensions, and pension expense, information about the fiduciary net position of the plan and additions to/deductions from the plan's fiduciary net position have been determined on the same basis as they are reported by OCERS. For this purpose, plan contributions are recognized when they are due and payable in accordance with plan terms. Investments are reported at fair value.

(k) Revenue Recognition

Toll revenue is recognized at the time the vehicle passes through the toll plaza. Other revenue is recognized when earned.

(l) Transactions with SJHTCA

As described in note 7(e), payments of $120,000 to SJHTCA through 2009 that were originally recorded as construction in progress have been reclassified as a note receivable from SJHTCA and a reduction of construction in progress in 2015.

Expenses directly related entirely to the agency are charged to the agency, and those incurred on behalf of both the agency and SJHTCA are allocated between the two agencies based on the estimated benefit to each. In addition, the agency has amounts due from SJHTCA related to SJHTCA customers who incur tolls on the agency's corridors and other expenses and amounts due to SJHTCA related to the agency's customers who incur tolls on State Route 73. At June 30, 2015, the agency had a net payable to SJHTCA of $6,444.

(m) Net Position

The agency's net position is classified within the following categories:

Net investment in capital assets: Represents the agency's capital assets, net of accumulated depreciation and the outstanding principal balances of debt attributable to the acquisition, construction, and improvement of those assets.

Restricted: Represents the agency's assets subject to externally imposed conditions, related primarily to restricted bond proceeds and certain revenue collected, net of related liabilities.

Unrestricted: Represents the remainder of the agency's net position not included in the categories above.

(n) Use of Estimates

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of certain assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates.

(In thousands)

(3) Development Impact Fees

The sources of development impact fees for the year ended June 30, 2015 were as follows:

City of Irvine	$	19,368
City of Lake Forest		2,416
County of Orange		1,016
City of Yorba Linda		658
City of San Juan Capistrano		612
City of Tustin		338
City of Mission Viejo		284
City of San Clemente		117
City of Anaheim		52
City of Santa Ana		30
City of Rancho Santa Margarita		6
City of Orange		4
	$	24,901

(4) Cash and Investments

Cash and investments as of June 30, 2015 are classified in the accompanying financial statements as follows:

Current cash and investments	$	76,833
Noncurrent cash and investments		74,515
Current restricted cash and investments		141,926
Noncurrent restricted cash and investments		261,854
	$	555,128

(In thousands)

Cash and investments as of June 30, 2015 consist of the following:

	Cash and cash equivalents	Investments	Total
Cash on hand	$ 2	—	2
Deposit accounts	15,224	995	16,219
Money market funds	7,425	—	7,425
Commercial paper	—	27,980	27,980
U.S. Treasury securities	—	36,858	36,858
Federal agency securities	24,599	59,234	83,833
State and local bonds	—	11,936	11,936
Corporate notes	—	11,076	11,076
Investments held with trustee per debt agreements:			
Money market funds	34,359	—	34,359
Commercial paper	—	4,563	4,563
U.S. Treasury securities	—	189,057	189,057
Federal agency securities	47,998	83,822	131,820
Total	$ 129,607	425,521	555,128

(a) Cash Deposits

Custodial Credit Risk Related to Cash Deposits

Custodial credit risk for deposits is the risk that, in the event of failure of a depository financial institution, the agency will not be able to recover its deposits or will not be able to recover collateral securities that are in possession of an outside party.

At June 30, 2015, the carrying amount of the agency's cash deposits was $15,224 and the corresponding aggregate bank balances were $16,125. The difference of $901 was principally due to outstanding checks. The agency's custodial credit risk is mitigated in that the full amounts of the bank balances outlined above were insured by federal depository insurance or collateralized in accordance with Section 53652 of the California Government Code with securities held by the pledging financial institution in the agency's name.

(b) Investments

Credit Risk and Concentration of Credit Risk

Credit risk is the risk that an issuer or other counterparty to an investment will not fulfill its obligations. Concentration of credit risk is the risk of loss attributed to the magnitude of an investment in a single issuer. The agency mitigates these risks by holding a diversified portfolio of high-quality investments.

The agency's investment policy sets specific parameters by type of investment for credit quality, maximum maturity, and maximum percentage investment. Both the policy and the agency's debt agreements generally require that all securities must be issued by companies with a long-term debt rating of at least "A" by two of the Nationally Recognized Statistical Rating Organizations (NRSRO) or at least "AA" by one NRSRO. The policy also indicates specific rating requirements for certain types of investments. Further, there are percentage limitations on the purchase of specific types of securities, based on the purchase price of the security as compared to the market value of the total portfolio at the time of purchase. However, the policy does not require sales of individual securities due to subsequent changes in market value that cause their values to exceed the prescribed maximum percentages of the portfolio.

The table below identifies the types of investments that are authorized by the agency's investment policy and certain provisions of the agency's policy that address interest rate risk and concentration of credit risk. This table does not address investments of debt proceeds held by the bond trustee, which are governed by the provisions of the agency's debt agreements rather than by the agency's investment policy.

Authorized investment type		Maximum maturity	Maximum percentage of portfolio*	Maximum percentage investment in one issuer	Specific rating requirement
U.S. Treasury bills, notes, and bonds		5 years	100	100	N/A
Federal agency and U.S. government-sponsored enterprise notes and bonds		5 years	100	35	N/A
Federal agency mortgage-backed securities		5 years	20	15	2nd highest ratings category by an NRSRO
Certificates of deposit	**	5 years	100	5	Long-term debt rating in one of highest ratings categories by two NRSROs
Certificates of Deposit Account Registry Service		5 years	30	5	Long-term debt rating in one of highest ratings categories by two NRSROs

(In thousands)

Authorized investment type	Maximum maturity	Maximum percentage of portfolio*	Maximum percentage investment in one issuer	Specific rating requirement
Negotiable certificates of deposit	5 years	30	5	Long-term debt rating in one of highest ratings categories by two NRSROs
Banker's acceptances	180 days	30	5	Drawn on and accepted by a bank that carries the highest short-term ratings category by one NRSRO
Commercial paper	270 days	25	Lesser of 5% of portfolio or 10% of outstanding paper of issuer	Highest short-term rating by an NRSRO
Repurchase agreements	90 days	25	5	N/A
Medium-term maturity corporate notes	5 years	30	5	Long-term debt rating in one of highest ratings categories by two NRSROs
State of California Local Agency Investment Fund	N/A	Lesser of $50 million or 15% of portfolio	5	N/A
County or local agency investment pools	N/A	15	5	N/A
Shares in a California common law trust	N/A	20	5	Highest rating category by an NRSRO
Asset-backed securities	5 years	20	5	Highest rating by one NRSRO; issuer must also have one of the three highest ratings from two NRSROs

Authorized investment type	Maximum maturity	Maximum percentage of portfolio*	Maximum percentage investment in one issuer	Specific rating requirement
Money market mutual funds	N/A	20	5	Highest applicable rating by two NRSROs
Bonds or notes issued by the State of California, any local agency in the state, or any other state	5 years	30	5	One of the three highest rating categories by at least two NRSROs

* Excluding amounts held by trustee, which are subject to provisions of the bond indentures.

** The full amounts of principal and accrued interest must be insured by the Federal Deposit Insurance Corporation (FDIC) or the National Credit Union Administration (NCUA).

The investment of debt proceeds and toll revenue held by the agency's bond trustee is governed by provisions of the debt agreements, rather than by the general provisions of the California Government Code or the agency's investment policy. The following table identifies the investment types that are authorized for these funds, and if applicable, the specific rating requirements:

Investments authorized by debt agreements	Specific rating requirement
U.S. Government obligations	N/A
U.S. Federal agency debt instruments	N/A
State and local government debt securities	One of the two highest rating categories by Moody's and S&P, and if rated by Fitch, in one of the two highest rating categories
Certificates of deposit, savings accounts, deposit accounts, or money market deposits insured by the Federal Deposit Insurance Corporation (FDIC)	N/A
Certificates of deposit collateralized by U.S. government or federal agency obligations	N/A
Federal funds or bankers' acceptances	Prime-1 or A3 or better by Moody's, A-1 or A or better by S&P and, if rated by Fitch, F-1 or A or better

Investments authorized by debt agreements		Specific rating requirement
Commercial paper		Prime-1 or better by Moody's and A-1 or better by S&P and, if rated by Fitch, F-1 or better
Repurchase agreements with terms up to 30 days, secured by U.S. government or federal agency obligations		A or better by both Moody's and S&P and, if rated by Fitch, A or better
Medium-term corporate notes with maximum maturity of five years		One of the three highest applicable rating categories, or approved in writing, by S&P, and, if rated by Fitch, one of the three highest applicable rating categories
Money market mutual funds		AAAm-G, AAA-m, or AA-m by S&P and, if rated by Moody's, Aaa, Aa1 or Aa2 and, if rated by Fitch, AAA or AA
Investment agreements	*	N/A

* Investments may be allowed if the agency certifies to the trustee that the investment was approved in writing by each rating agency, which has assigned a rating to the agency's bonds, and by the agency's bond insurer.

At June 30, 2015, all of the agency's investments were rated at or above the minimum levels required by its investment policy and its debt agreements, as shown below:

Investment type	S&P	Moody's
U.S. Treasury bills	AA+	Aaa
U.S. Treasury notes	AA+	Aaa
U.S. Treasury strips	AA+	Aaa
U.S. federal agency bonds *	AA+/A-1+	Aaa/P-1
Money market funds	AAAm	—
Commercial paper:		
Rabobank USA Fin Corp	A-1	P-1
Abbey National North America	A-1	P-1
General Electric Capital	A-1+	P-1
Toyota Motor Credit Corp	A-1+	P-1
Corporate notes – Medium term:		
New York Life	AA+	Aaa
United Health Group	A+	A3

(In thousands)

Investment type	S&P	Moody's
State and local bonds:		
San Francisco Bay Area Toll Authority	AA	Aa3
New York State Urban Development	AAA	Aa1
University of California Regents Revenue	AA	Aa2

* Ratings are indicated to the extent available. However, in some instances, discounted federal agency bonds are not rated.

Custodial Credit Risk

Custodial credit risk for investments is the risk that the agency will not be able to recover the value of investment securities that are in the possession of an outside party. All securities owned by the agency are deposited in the agency's trustee bank with the exception of a money market account that is deposited in the agency's primary bank. Securities are not held in broker accounts.

Interest Rate Risk

Interest rate risk is the risk that changes in interest rates will adversely affect the fair value of an investment. The agency mitigates this risk by matching maturity dates, to the extent possible, with the agency's expected cash flow.

A summary of the agency's investments held at June 30, 2015 that are governed by the agency's investment policy and its bond agreements, including money market funds of $41,784 and federal agency securities of $72,597 that are considered cash equivalents, is as follows:

			Remaining maturity (in years)			
Investment type		**Fair value**	**Less than one**	**One to two**	**Two to five**	**More than five**
U.S. Treasury notes	$	225,915	18,226	133,301	74,388	—
Money market funds		41,784	41,784	—	—	—
Federal agency securities		215,653	131,485	54,094	30,074	—
Commercial paper		32,543	32,543	—	—	—
Corporate notes		11,076	5,001	6,075	—	—
State and local bonds		11,936	11,936	—	—	—
Certificates of deposit		995	995	—	—	—
Total	$	539,902	241,970	193,470	104,462	—

At June 30, 2015, with the exception of investments issued or explicitly guaranteed by the U.S. government and money market mutual funds, there were no investments in any issuers that accounted for 5% or more of the agency's total investments, other than investments with Federal Home Loan Bank, Federal Home Loan Mortgage Corporation, and Federal National Mortgage Association that represented 17%, 9%, and 8%, respectively, of the agency's total investments, as permitted by the agency's investment policy and the applicable bond indentures.

(In thousands)

(5) Capital Assets

Capital assets activity for the year ended June 30, 2015 was as follows:

		Balance at beginning of year	Additions	Transfers/ deletions	Balance at end of year
Construction in progress	$	346,643	35,531	(134,372)	247,802
Right-of-way acquisitions, grading, or improvements		15,014	—	—	15,014
Furniture and equipment		39,352	5,066	(1,331)	43,087
		401,009	40,597	(135,703)	305,903
Accumulated depreciation		(16,666)	(4,902)	1,331	(20,237)
	$	384,343	35,695	(134,372)	285,666

Right-of-way acquisitions, grading, and improvements include easements and environmental mitigation parcels. Furniture and equipment include transponders, toll and violations collection equipment, buildings, vehicles, and leasehold improvements.

Transfers/Deletions

During the year ended June 30, 2015, the agency completed its All Electronic Tolling (AET) conversion project and expenditures of $2,688 related to the installation of new toll equipment were transferred from construction in progress.

Ownership of the Foothill/Eastern Transportation Corridor construction, rights-of-way, grading, and improvements was transferred to Caltrans during the year ended June 30, 1999 upon satisfaction of all conditions contained within the Cooperative Agreements between the agency and Caltrans. The agency incurs additional costs for improvements and enhancements to the thoroughfares previously transferred to Caltrans. These improvements and enhancements are covered by separate project-specific Cooperative Agreements with Caltrans. They are transferred to Caltrans on an ongoing basis and recognized as contribution expense; expenses of $11,684 were recognized during the year ended June 30, 2015. The balance of construction in progress at June 30, 2015 represents additional capital improvements, primarily including the 241 completion project, which will also be transferred to Caltrans upon completion.

As described in note 7(e), payments of $120,000 to SJHTCA through 2009 that were originally recorded as construction in progress have been reclassified in 2015 and reflected as a note receivable from SJHTCA and a reduction of construction in progress.

(In thousands)

(6) Long-Term Obligations

Following is a summary of changes in long-term obligations during the year ended June 30, 2015:

	Balance at beginning of period	Additions/ accretions	Reductions	Balance at end of period	Due within one year
Series 2013 Toll Road Refunding Revenue Bonds:					
Current Interest Bonds	$ 1,947,490	—	—	1,947,490	—
Capital Appreciation Bonds	135,083	8,259	—	143,342	—
Convertible Capital Appreciation Bonds	201,770	12,472	—	214,242	—
Series 2015 Toll Road Refunding Revenue Bonds:					
Capital Appreciation Bonds	—	88,363	—	88,363	—
Series 1995A Senior Lien Toll Road Revenue Bonds:					
Current Interest Bonds	179,990	—	(179,990)	—	—
Total bonds payable	2,464,333	109,094	(179,990)	2,393,437	—
Less unamortized discount on 2013 bonds	(40,814)	—	416	(40,398)	
Total bonds payable less unamortized discount	$ 2,423,519	109,094	(179,574)	2,353,039	

In February 2015, the agency issued $87,008 of Senior Lien Toll Road Refunding Revenue Bonds (2015 Capital Appreciation Bonds); together with certain funds held in trust, the proceeds of the issuance were used to refund the previously unrefunded portion of the Series 1995A Senior Lien Toll Road Revenue Bonds, at par value plus accrued interest. In connection with this transaction, the agency realized an economic gain (as measured by the difference in present value of the scheduled debt service payments on the old and new debt) of approximately $34 million. In addition, the agency incurred bond insurance premiums of $1,360 related to a portion of the bonds, which is being amortized over the life of those bonds, and other transaction costs of $2,061, which has been recorded as expense.

In December 2013, the agency issued $2,274,617 of Series 2013 Toll Road Refunding Revenue Bonds (2013 Bonds); the proceeds of the issuance were used to refund the outstanding balance of the 1999 Bonds. The reacquisition price of the refunded bonds exceeded their net carrying amount by $14,534; this amount was considered a deferred loss for accounting purposes and is being amortized through 2040, the remaining period during which the refunded bonds were scheduled to be repaid. In addition, the agency incurred bond insurance premiums of $9,533, which is being amortized over the life of the 2013 bonds. The 2013 Bonds were issued at a discount of $41,009, which is being amortized over the life of the bonds.

(Continued)

The 2013 current interest bonds include $1,374,440 of Senior Term Bonds that mature in installments from January 2042 through January 2053; $375,000 of Term Rate Bonds that mature in installments from January 2050 through January 2053; and $198,050 of Junior Lien Bonds that mature in installments from January 2023 through January 2043. Interest on the 2013 current interest bonds is payable semiannually at rates ranging from 5.00% to 6.50%. The Senior Term Bonds and the Junior Lien Bonds are subject to early redemption on or after January 15, 2024, at the option of the agency, by payment of principal and accrued interest. The Term Rate Bonds are subject to early redemption, at the option of the agency, by payment of principal and accrued interest, on or after the dates ranging from July 15, 2017 through July 15, 2022.

The 2013 capital appreciation bonds accrue interest at rates ranging from 3.75% to 7.125%, compounded semiannually, and are scheduled to mature in annual installments from January 2020 to January 2042. The bonds are subject to early redemption, at the option of the agency, based on an independent make-whole calculation.

The 2013 convertible capital appreciation bonds accrue interest, compounded semiannually based on accreted amounts, at rates ranging from 5.30% to 6.85% through January 15, 2024. After this date, interest is payable semiannually based on accreted amounts. The bonds are scheduled to mature in annual installments from January 2025 to January 2042. The bonds are subject to early redemption on or after January 15, 2031, at the option of the agency, by payment of the accreted amounts and accrued interest.

The master indentures of trust require the trustee to hold bond proceeds, toll revenue, and any other proceeds included in pledged funds for debt service. These moneys are included in the restricted cash and investments held by the trustee.

(Continued)

(In thousands)

Following is a summary of the annual debt service requirements by fiscal year for the agency's long-term debt obligations as of June 30, 2015:

		Principal	Interest[(1)]	Total
2016	$	—	112,770	112,770
2017		—	112,770	112,770
2018		—	112,770	112,770
2019		—	112,770	112,770
2020		3,938	113,494	117,432
2021–2025		41,314	610,142	651,456
2026–2030		86,646	695,528	782,174
2031–2035		193,847	745,830	939,677
2036–2040		215,967	890,392	1,106,359
2041–2045		522,050	570,168	1,092,218
2046–2050		759,185	271,930	1,031,115
2051–2053		570,490	48,179	618,669
	$	2,393,437	4,396,743	6,790,180

(1) Includes payments scheduled on January 1 and January 15 of the indicated fiscal year and July 1 and July 15 of the following fiscal year, to coincide with the annual debt service calculations used for covenant compliance purposes.

Included in principal at June 30, 2015 is $31,813 related to accreted principal on convertible capital appreciation bonds and capital appreciation bonds.

The net proceeds of the 1999 Bonds plus additional 1995 Series moneys were used to purchase U.S. government securities, which were placed in an irrevocable escrow fund to be used for the debt service payments related to a previously refunded portion of the 1995 bonds. As of June 30, 2015, the amount of the previously refunded 1995 bonds outstanding, which were previously eliminated from the financial statements as a result of the refunding, was $753,132.

(7) Commitments and Contingencies

(a) Toll Collection and Revenue Management System Agreements

The agency and SJHTCA have entered into agreements with contractors for various services, including toll collection systems operation and maintenance. The agreements expire on various dates through June 30, 2025 and are cancelable by the agency, without further obligation, with advance written notice.

(b) Project Costs

As of June 30, 2015, the agency has outstanding commitments and contracts for improvements on existing construction of approximately $13,218.

(c) Litigation

The agency is a defendant in various legal actions. Management believes that the ultimate resolution of these actions will not have a significant effect on the agency's financial position or results of operations.

(d) Risk Management

The agency maintains insurance coverage for various risks, including but not limited to property, liability, earthquake, and flood coverage. Coverage is purchased in accordance with the agency's master indentures of trust, as applicable.

(e) Mitigation Payment and Loan Agreement

On November 10, 2005, the agency's Board of Directors and the Board of Directors of SJHTCA, entered into a Mitigation Payment and Loan Agreement (the Agreement). The terms of the Agreement called for the agency to make payments totaling $120,000 over four years to SJHTCA to mitigate for anticipated loss of revenue due to the construction of the 241 completion project. All scheduled payments totaling $120,000 were made to SJHTCA as of June 2009 and were recorded as construction in progress.

In addition, the agency committed to provide loans to SJHTCA on an as-needed basis up to $1,040,000, subject to the terms of the Agreement, to assist SJHTCA in achieving its required debt service coverage ratio. Payments of accrued interest and outstanding principal would begin in the fiscal year when SJHTCA achieved a surplus in revenue in excess of the amount needed to meet the debt coverage requirement. All principal and accrued interest would be due and payable on January 1, 2037 to the extent that SJHTCA had surplus revenue available to pay all amounts due. The Agreement also stipulated that the agency would not be obligated to make loans to SJHTCA prior to securing the necessary funds for constructing the 241 completion project unless the agency determined that it would not build the project. If the commencement and diligent pursuit of the construction of the 241 completion project did not occur by June 30, 2015, the mitigation payments would be added to the principal amount of the loan. No amounts were loaned in connection with this arrangement.

On August 14, 2014, the agency's Board of Directors and the Board of Directors of SJHTCA approved an agreement that provided for termination of the Mitigation Payment and Loan Agreement concurrently with the closing of a refinance transaction proposed by SJHTCA. The closing of this refinance transaction occurred on November 6, 2014. The termination agreement also provided for SJHTCA to pay $120,000 to the agency, in annual installments beginning January 15, 2025 equal to 50% of SJHTCA's surplus funds as defined in the agreement. Interest accrual based on the average annual yield of the State of California Pooled Money Investment Account commenced upon closing of the transaction and interest is payable annually beginning January 15, 2025.

As a result of this agreement, the aggregate payments of $120,000 that were made to SJHTCA through 2009 have been reclassified as a note receivable from SJHTCA and a reduction of construction in progress.

(Continued)

(8) Corridor Operations Facility Lease

In January 2000, the agency, along with SJHTCA, relocated to the corridor operations facility. At that time, a lease agreement was executed between the agency (lessor) and SJHTCA (lessee). The lease agreement expires at the earliest occurrence of 1) dissolution of the agency, 2) sale of the facility, or 3) dissolution of SJHTCA. Lease payments are based on the estimated fair market rental value and are adjusted annually. The agency received lease revenue for the year ended June 30, 2015 of $386.

(9) Employees' Retirement Plans

Defined Benefit Plan – Qualified permanent employees of the agency participate in a cost-sharing multiple-employer defined benefit pension plan administered by OCERS, a public employee retirement system established in 1945. The Plan is subject to the provisions of the County Employees Retirement Law of 1937 (California Government Code Section 31450 et. seq.); the California Public Employees' Pension Reform Act of 2013 (Government Code Section 7522 et. seq.); and other applicable statutes.

(a) Benefits

The Plan provides retirement, disability, and death benefits to eligible plan members and their beneficiaries. Monthly retirement benefits are determined by benefit formulas that depend upon the classification of employees; the date of entering membership in OCERS or a reciprocal plan; retirement age; years of service; and final average compensation. The agency's members hired prior to January 1, 2013 are subject to a benefit formula of 2.0% of final average compensation per year of service, based upon retirement at age 55. Members hired on or after January 1, 2013 are subject to a benefit formula of 2.5% at 67.

Amounts payable for retired members are subject to annual cost-of-living adjustments based upon changes in the Consumer Price Index for the prior calendar year. Adjustments are limited to a maximum increase or decrease of 3% per year.

(b) Contributions

Employer and employee contribution requirements are determined as percentages of covered payroll amounts and vary based upon the age of each employee at the date of entering membership in OCERS or a reciprocal plan. Employer contribution rates are determined using the entry age normal actuarial cost method based upon a level percentage of payroll. For the year ended December 31, 2014, employer contribution rates ranged from 21.04% to 57.28%. Employee contributions are established by the OCERS Board of Retirement and guided by applicable state statutes. For the year ended December 31, 2014, employee contribution rates ranged from 8.93% to 15.63%. The amount of contributions from the agency recognized by the plan, measured as the total amount recognized as additions to the plan's fiduciary net position for the period ended December 31, 2014 and 2013, was $896 and $897, which was 100% of the required contribution, and represented 20.9% and 19.3% of the agency's covered-employee payroll, respectively.

(In thousands)

(c) Pension Liabilities, Pension Expense, and Deferred Outflows/Inflows of Resources

For purposes of reporting under GASB Statement No. 68, OCERS arranged for determination of the plan's collective net pension liability; deferred outflows and inflows of resources related to pensions; and pension expense, as well as the proportionate share of each amount applicable to the plan's participating employers, using measurement dates of December 31, 2014 and 2013, with respective actuarial valuations as of December 31, 2013 and 2012 and standard procedures to roll forward to the respective measurement dates. The agency's reporting dates are June 30, 2015 and 2014. The proportionate shares of these amounts attributable to the Transportation Corridor Agencies have been determined by OCERS's actuary based upon actual employer contributions within each rate group and further allocated between the agency and SJHTCA on the basis of their respective shares of covered payroll to determine the amounts reportable by the agency, as indicated below:

			Percentage of collective amount	**Covered-employee payroll**
Collective net pension liability at December 31, 2014	$	5,082,481	100.00%	$ —
Proportionate share attributable to Transportation Corridor Agencies		10,683	0.21%	6,121
Share allocable to Foothill/ Eastern Transportation Corridor Agency		7,556	0.15%	4,289

Agency's share of collective net pension liability as a percentage of its covered-employee payroll	176%
Plan's fiduciary net position as a percentage of the total pension liability	69.42%

(In thousands)

			Percentage of collective amount		Covered-employee payroll
Collective net pension liability at December 31, 2013	$	5,291,126	100.00%	$	—
Proportionate share attributable to Transportation Corridor Agencies		11,359	0.21%		6,551
Share allocable to Foothill/ Eastern Transportation Corridor Agency		8,039	0.15%		4,636

Agency's share of collective net pension liability as a percentage of its covered-employee payroll	173%
Plan's fiduciary net position as a percentage of the total pension liability	67.16%

Collective deferred outflows of resources at December 31, 2014	$	389,055
Proportionate share attributable to Transportation Corridor Agencies		453
Share allocable to Foothill/Eastern Transportation Corridor Agency		317
Collective deferred inflows of resources at December 31, 2014	$	538,504
Proportionate share attributable to Transportation Corridor Agencies		1,443
Share allocable to Foothill/Eastern Transportation Corridor Agency		1,011
Collective pension expense for the year ended June 30, 2015	$	566,324
Proportionate share attributable to Transportation Corridor Agencies		1,594
Share allocable to Foothill/Eastern Transportation Corridor Agency		1,117

The agency's deferred outflows of resources related to pensions as of June 30, 2015 are attributable to the following:

Net difference between projected and actual earnings on pension plan investments	$	317
Contributions to the plan subsequent to the measurement date of the collective net pension liability		560
Total deferred outflows related to pensions	$	877

(In thousands)

The agency's deferred inflows of resources related to pensions as of June 30, 2015 are attributable to the following:

Differences between expected and actual experience	$	444
Changes of assumptions or other inputs		567
Total deferred inflows related to pensions	$	1,011

The amount of $560 representing the agency's balance of deferred outflows of resources related to contributions subsequent to the measurement date will be recognized as a reduction of the net pension liability in the year ending June 30, 2016. The other amounts of the agency's balances of deferred outflows and deferred inflows of resources as of June 30, 2015 will be recognized in pension expense as follows:

Year ending June 30:		
2016	$	116
2017		116
2018		116
2019		116
2020		195
2021		35
	$	694

(d) Actuarial Assumptions and Other Inputs

The following significant methods and assumptions were used to measure the plan's total pension liability as of December 31, 2014 and 2013:

- Actuarial experience study – Three-year period ended December 31, 2013
- Inflation rate – 3.00% for 2014; 3.25% for 2013
- Projected salary increases – 4.25% to 17.50% for 2014; 4.75% to 17.75% for 2013, depending upon service and nature of employment
- Cost of living adjustments – 3.00%

The mortality assumptions for December 31, 2014 were based on the results of the actuarial experience study for the period January 1, 2011 through December 31, 2013 using the RP-2000 Combined Healthy Mortality Table projected with the Society of Actuaries Scale BB to 2020. The mortality assumptions for December 31, 2013 were based on the results of the actuarial experience study for the period January 1, 2008 through December 31, 2010 using the RP-2000 Combined Healthy Mortality Table. The mortality assumptions were then customized to account for the plan's membership experience.

(Continued)

(In thousands)

The discount rate used to measure the plan's total pension liability of December 31, 2014 and 2013 was 7.25%. The projection of cash flows used to determine the discount rate assumed that plan member contributions will be made at the current contribution rates and that employer contributions will be made at actuarially determined rates. Based on those assumptions, the plan's fiduciary net position was projected to be available to make all projected future benefit payments for current plan members. Therefore, the long-term expected rate of return on plan investments was applied to all periods of projected benefit payments to determine the total pension liability. The long-term expected rate of return should be determined without reduction for plan administrative expense. The 7.25% investment return assumption is net of administrative expenses, assumed to be 16 basis points. The long-term expected rate of return on plan investments was determined using a building-block method in which best-estimate ranges of expected future real rates of return are developed for each major asset class. These returns are combined to produce the long-term expected rate of return by weighting the expected future real rates of return by the target asset allocation percentages and by adding expected inflation and deducting expected investment expenses.

The target allocation and projected arithmetic real rate of return for each major asset class, after deducting inflation but before deducting investment expenses, used in the derivation of the long-term expected rate of return assumption are summarized in the following table:

		Target allocation	Long-term expected real rate of return
Asset class:			
Large Cap U.S. Equity	$	14.90%	5.92%
Small/Mid Cap U.S. Equity		2.73	6.49
Developed International Equity		10.88	6.90
Emerging International Equity		6.49	8.43
Core Bonds		10.00	0.73
Global Bonds		2.00	0.30
Emerging Market Debt		3.00	4.00
Real estate		10.00	4.96
Diversified Credit (U.S.)		8.00	4.97
Diversified Credit (Non-U.S.)		2.00	6.76
Hedge Funds		7.00	4.13
GTAA		7.00	4.22
Real return		10.00	5.86
Private equity		6.00	9.60
Total	$	100.00%	

(Continued)

(In thousands)

The following table presents the agency's proportionate share of the plan's net pension liability as of December 31, 2014, calculated using the discount rate of 7.25%, as well as what its proportionate share of the net pension liability would be if it were calculated using a discount rate one percentage point lower (6.25%) or one percentage point higher (8.25%) than the current discount rate:

Net pension liability, calculated using:		
With current discount rate of 7.25%	$	7,556
With a 1% decrease, to 6.25%		10,941
With a 1% increase, to 8.25%		4,644

(e) Plan's Fiduciary Net Position

OCERS provides publicly available financial information, including comprehensive annual financial reports and actuarial valuations, on the following website: www.ocers.org. Detailed information about the plan's fiduciary net position is included in the comprehensive annual financial report for the fiscal year ended December 31, 2014, which may also be obtained by calling (714) 558-6200.

(f) Employee Contributions

As described above, plan members contribute a percentage of their annual covered salaries at actuarially determined rates based on the age of entry into the plan. For employees who were hired prior to January 1, 2013, the agency paid up to 7% of each employee's required contribution through June 30, 2013. However, this percentage was reduced to 4.5% as of July 1, 2013 and to 2.0% as of July 1, 2014. As of July 1, 2015, the agency's payments toward the employees' required contributions have been fully eliminated. In addition to the pension expense determined in accordance with the requirements of GASB No. 68 as described above, the agency incurred expense of $62 for the year ended June 30, 2015 related to its subsidization of employee contributions.

Defined Contribution Plan – The agency also sponsors a defined contribution plan under the provisions of Internal Revenue Code Section 457 that permits employees to defer portions of their pre-tax compensation. The agency provides matching contributions to a related Section 401(a) plan, at a rate of 50% of the employees' deferral contributions, up to a maximum of 2% of each employee's related compensation. In connection with this plan, the agency incurred $57 of expense for the year ended June 30, 2015.